TD 94/10 - Income tax: can a taxpayer after lodging a return but before any assessment is made alter the figure for closing stock by adopting a different basis of valuation to that on which the return was originally prepared?

Taxation Determination

Income tax: can a taxpayer after lodging a return but before any assessment is made alter the figure for closing stock by adopting a different basis of valuation to that on which the return was originally prepared?

1. Subsection 31(1) of the *Income Tax Assessment Act 1936* allows a taxpayer the option of valuing each article of trading stock on hand at the end of the year of income at cost price, market selling value or the price at which it can be replaced. Although the provision is silent on the method and timing for exercising the option, it is necessary for a taxpayer to choose the method of valuation in order to ascertain whether or not there is a taxable income for a particular year.

2. It is considered that the valuation option is exercised at the time the taxpayer ascertains whether or not there is taxable income. The method chosen will be evident in the taxpayer's calculation of taxable income or loss as specified in the tax return. By making the choice the taxpayer is electing what law is to be applied in ascertaining the value of trading stock, which must be taken into account in determining taxable income.

3. Where a taxpayer chooses a method of valuation that is appropriate to the business and the Commissioner makes an assessment of taxable income and tax payable thereon, or is deemed to have made an assessment under section 166A, a taxpayer cannot vary the method of valuation. Any post assessment alteration to the method used to value closing stock can only be made by amending the assessment. The Commissioner will not accede to a taxpayer's request for an amendment to alter taxable income so that it reflects a different method of valuation. Nor will the Commissioner allow any part of an objection to an assessment that it is grounded on the taxpayer's desire to choose a different method of valuation. This is because an assessment made in reliance on a taxpayer's chosen method of valuation, would have been made on a correct basis by applying the law properly to the facts as disclosed by the taxpayer.

4. Where a taxpayer has lodged a return but no assessment has been made, as in the case of a loss company, it is open for the Commissioner to accept a request from a taxpayer to vary the information disclosed in the return. The Commissioner will allow a taxpayer to choose a different method of valuation of closing stock to that originally chosen at any time before an assessment is made. A taxpayer choosing a different method of valuation must use that value as the value of trading stock at the beginning of the following year of income.

Example 1

Jarrah Pty Ltd carries on a business of manufacturing furniture. In calculating its income from trading for the year ended 30 June 1993 the company valued its closing stock of timber at $25,000, ie the price at which it can be replaced. In that particular year it did not have a taxable income but made a $4,000 loss. Following lodgment of its return the company realised that it had claimed a deduction of $5,000 for legal expenses that were of a capital nature. Making an adjustment to exclude this deduction would give rise to a taxable income of $1,000. The company wanted to offset this adjustment by reducing the value of its closing stock. This could be achieved by choosing the cost price method to give a valuation of $20,500. The net result would be a loss for the year of $3,500.

The Commissioner will allow the taxpayer to choose the different method of valuation. The taxpayer should advise the Commissioner of the changes to its income derived during the year and the deductions and losses claimed.

Example 2

Snow Pty Ltd carries on a business of retailing ski equipment. In calculating its income from trading for the year ended 30 June 1991 the company valued its closing stock of skis at $45,000, ie the market selling value. In that particular year it did not have a taxable income but made a $6,000 loss. In 1993 a taxation audit was conducted into the company. It was advised that adjustments would be made disallowing $14,000 in deductions incurred on overseas travel by the directors. This would give rise to a taxable income of $8,000. The company advised the auditors that it wanted to offset the effect of this adjustment by choosing to value its closing stock at cost price, which was a figure of $35,000. The net result would be a loss for the year of $2,000.

The Commissioner will allow the taxpayer to choose the different method of valuation and this will be taken into account in determining whether or not the taxpayer has a taxable income.

Commissioner of Taxation
27/1/94

FOI INDEX DETAIL: Reference No. I 1216975 Previously issued as Draft 93/D249
Related Determinations:
Related Rulings:
Subject Ref: trading stock; closing stock valuation
Legislative Ref: ITAA 29; 31(1)
Case Ref:
ATO Ref: NAT 93/4918-9

ISSN 1038 - 8982